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CABINET AFFAIRS STAFFING MEMORANDUM

Date: 5-15-85 Number: 169164CA Due By:

Subject: Meeting of the Economic Policy Council - May 15th, 1985, 2:00 P.M.

Agenda Items: Post Summit Trade Strategy; Minimum Funding Waivers

ALL CABINET MEMBERS	Action	FYI		Action	FYI
Vice President	<input type="checkbox"/>	<input type="checkbox"/>	CEA	<input checked="" type="checkbox"/>	<input type="checkbox"/>
State	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	CEQ	<input type="checkbox"/>	<input type="checkbox"/>
Treasury	<input checked="" type="checkbox"/>	<input type="checkbox"/>	OSTP	<input type="checkbox"/>	<input type="checkbox"/>
Defense	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Attorney General	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interior	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Agriculture	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Commerce	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Labor	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
HHS	<input type="checkbox"/>	<input type="checkbox"/>	Saker	<input type="checkbox"/>	<input type="checkbox"/>
HUD	<input type="checkbox"/>	<input type="checkbox"/>	Beaver CHEW	<input type="checkbox"/>	<input type="checkbox"/>
Transportation	<input type="checkbox"/>	<input type="checkbox"/>	Berman (For WH Staffing)	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Energy	<input type="checkbox"/>	<input type="checkbox"/>	McFarlane	<input type="checkbox"/>	<input type="checkbox"/>
Education	<input type="checkbox"/>	<input type="checkbox"/>	Svahn	<input type="checkbox"/>	<input type="checkbox"/>
Counsellor	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OMB	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
CIA	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
UN	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
USTR	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
GSA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
EPA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
NASA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OPM	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
VA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
SBA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
			Executive Secretary for:		
			CCCT	<input type="checkbox"/>	<input type="checkbox"/>
			CCEA	<input type="checkbox"/>	<input type="checkbox"/>
			CCFA	<input type="checkbox"/>	<input type="checkbox"/>
			CCHR	<input type="checkbox"/>	<input type="checkbox"/>
			CCLP	<input type="checkbox"/>	<input type="checkbox"/>
			CCMA	<input type="checkbox"/>	<input type="checkbox"/>
			CCNRE	<input type="checkbox"/>	<input type="checkbox"/>

REMARKS:

The first meeting of the Economic Policy Council will be Thursday May 16, 1985, at 2:00 P.M., in the Roosevelt Room.

The background papers are attached.

Attendance will be limited to principals only.

RETURN TO:

☐ Craig L. Fuller
Assistant to the President
for Cabinet Affairs
456-2823 (White House)

☐ Don Clarey
☒ Tom Gibson
☐ Larry Herbolsheimer

Associate Director

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EXEC
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THE WHITE HOUSE

WASHINGTON

May 14, 1985

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: ROGER B. PORTER *RBP*

SUBJECT: Agenda and Papers for the May 16 Meeting

The agenda and papers for the May 16 meeting of the Economic Policy Council are attached. The meeting is scheduled for 2:00 p.m. in the Roosevelt Room.

The first agenda item is a discussion of trade strategy following the Bonn Economic Summit. A paper prepared by the Office of the U.S. Trade Representative outlining a proposed post-Bonn Summit trade strategy is attached.

The second agenda item concerns minimum funding waivers. At its March 29 meeting, the Cabinet Council on Economic Affairs reviewed the issue of minimum funding waivers for defined benefit pension plans. The Council requested that the Working Group on Pension Policy prepare an options paper on the minimum funding waiver issue. In the intervening weeks the Working Group has met on several occasions. A paper on this issue is also attached.

Attachments

THE WHITE HOUSE
WASHINGTON

ECONOMIC POLICY COUNCIL

May 16, 1985

Roosevelt Room

2:00 p.m.

AGENDA

1. Post Summit Trade Strategy
2. Minimum Funding Waivers

THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON
20506

May 10, 1985

MEMORANDUM TO ROGER PORTER

FROM: Michael B. Smith, Acting ~~AS~~
SUBJECT: Post Summit Trade Strategy Paper

Per my discussion with Secretary Baker and you earlier this week, attached is a paper we have prepared outlining the post-Bonn Summit trade strategy. This is intended for EPC discussion next Thursday.

Attachment

Trade Strategy Following the Bonn Economic Summit

While the United States was successful in getting most of its partners at the Summit to endorse a 1986 date for starting the new round of multilateral trade negotiations (MTN), France was a singular exception. Mitterrand blocked consensus on this issue. Also, several weeks ago India led an effort on the part of some developing countries to block a consensus agreement on the IMF/IBRD Development Committee communique both endorsing the new round and calling for early preparations leading to such a round.

It is clear that nearly all of the developed countries and many developing countries actively support, or at least can go along with, a new round of trade negotiations. These countries recognize that such a round is essential in helping to stem the global tide of protectionism and in facilitating the renewed expansion of trade. From the U.S. perspective such negotiations are important not only to maintain the post-war momentum toward a more open international economy, but also to meet specific U.S. trade objectives. These objectives include, as agreed by the Trade Policy Committee at its meeting of March 13, the following:

- Improving the international trading system through a more effective safeguards code, more effective rules covering agricultural trade under GATT extension of the NTB codes negotiated in the Tokyo Round and improvement of the GATT dispute settlement process;

- Establishing new trade disciplines in the areas of services, high technology, intellectual property and investment; and
- Expanding market access in areas of priority economic interest to the United States, through the reduction of specific tariff and non-tariff barriers.

We cannot allow countries like France, India and Brazil to thwart the desire on the part of most other countries to further progress in creating a more open international trading environment. It is, in the interest of the world community as a whole that some form of negotiations begin as soon as feasible -- specifically, next year. Even if negotiations were not fully multilateral, they would advance the cause of reducing trade barriers and bringing pressure on the recalcitrants to join the process. We should pursue a multi-prong strategy, involving a continued push for the preparation and launching of new multilateral trade negotiations, the organization of plurilateral negotiations where participation by the full GATT membership proves impossible, and the active pursuit of bilateral negotiations such as our talks with Japan on access to that market and possible free trade area arrangements with Canada or other Pacific countries.

1. Preparations and Launching of Multilateral Trade Negotiations

Both OECD ministers and Summit leaders in Bonn agreed (a) a new

GATT round should begin as soon as possible and (b) a meeting of senior officials should take place in the GATT before the end of the summer to reach a broad consensus on subject matter and modalities for such negotiations. There will be a number of meetings in the GATT over the next few weeks to discuss the scheduling of a senior officials meeting, and Trade Ministers are scheduled to discuss the parameters of a new round of negotiations June 8-10 in Stockholm (by 16 developed and developing countries) and July 13-14 in Canada (the quadrilateral meeting of US, EC, Japan and Canada). The U.S. position at these meetings should be to push for a consensus in the GATT on a meeting of senior officials to discuss the agenda for a new round (we have proposed July 22 as the date) and to take advantage of upcoming multilateral and bilateral meetings (such as the visit of Prime Minister Gandhi) to build a consensus on the need for a new round and on the agenda for such a round.

2. Plurilateral Negotiations -

We may not be able to get all GATT countries to agree on the need for a new round of multilateral trade negotiations. In that case we should proceed with negotiations among those countries who are prepared to move forward. In anticipation of this possibility, both the OECD Ministerial Communique and the Summit Declaration noted the need for participation of a significant number of developed and developing countries (but not necess-

arily all GATT countries). Moreover, it is quite possible that a large number of developing countries could balk at the inclusion of some non-tariff topics of key importance to us (e.g., services, intellectual property, investment). In that case we should seek to pursue negotiations on such topics with like-minded countries who are prepared to move forward, leaving the door open for other countries to participate as observers and to join the agreement later. Such negotiations would proceed on a conditional MFN basis, the benefits of the agreement would accrue only to the participants. (The non-tariff codes on standards and procurement negotiated during the Tokyo Round are examples of this type of agreement.)

3. Bilateral Negotiations -

The United States also should take advantage of bilateral negotiating opportunities. The United States on a regular basis seeks to expand market access for U.S. products through bilateral talks with other countries. While our authority to make reciprocal concessions is circumscribed, continued access to our markets can be a formidable incentive for some countries to respond to our requests. We need to put particular emphasis, in this regard, in improving access to the Japanese and Korean markets.

The United States has negotiated previous bilateral free trade agreements, namely, the 1965 bilateral automobile agreement with

Canada and the recent free trade arrangement with Israel which is now going through the Congressional approval process. The Trade Act of 1984 gives us authority to negotiate similar arrangements with other countries, provided the Senate Finance Committee and House Ways and Means Committee give their approval. We have had preliminary discussions with Canada on possible bilateral free trade negotiations, most recently between Prime Minister Mulroney and President Reagan at the Quebec Summit. The Canadian Government is now holding domestic consultations in order to decide on a course of action, and they have told us that they plan to get back to us by late summer. We have also had a number of exploratory talks between Ambassador Brock and the ASEAN trade ministers on possible free trade arrangements and ASEAN is now keen to begin more serious discussions. New Zealand and Australia have both told us informally that they may be interested in pursuing exploratory talks; Korea has asked the Korean Development Institute to study the possibility of a bilateral free trade arrangement with us. In the year ahead, one or another of these countries could approach us with a request to initiate formal talks, and we therefore may well need to make a decision on whether to pursue these opportunities.

These bilateral negotiating opportunities could usefully complement any multilateral negotiations by giving us windows of opportunity for achieving higher levels of liberalization and higher degrees of commitment to market-oriented policies than is possible on a

broad multilateral basis. It could serve as a useful demonstration of the advantages of open-trade and market-oriented policies; and at the same time put pressure on others to support our multilateral initiatives. In the absence of multilateral negotiations, it could become a critical tool for deflecting protectionist pressures.

We recommend that we actively explore with the Pacific rim countries their interest in pursuing possible bilateral or regional free trade arrangements, in line with the President's statement to reporters at the Summit that the United States will have trade negotiations next year, whether it be multilaterally or bilaterally.

THE WHITE HOUSE

WASHINGTON

May 14, 1985

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: THE WORKING GROUP ON PENSION POLICY

SUBJECT: Minimum Funding Waivers

Issue

Should the Administration include as part of its proposed pension amendments a provision providing a statutory lien against an employer and in favor of plan beneficiaries when a minimum funding waiver is granted by the IRS?

Background

The 1974 ERISA law imposed minimum funding requirements on employers who maintain a defined benefit pension plan. The law authorizes the Secretary of the Treasury to waive minimum funding requirements so that companies with substantial business hardship can avoid terminating their pension plans. The Secretary has delegated this responsibility to the Internal Revenue Service.

The plan sponsor can receive minimum funding waivers for up to five years out of any consecutive fifteen year period. The word waiver is a misnomer in this case. A funding waiver is actually a deferral of all or part of the required yearly contribution; the deferred amount must be amortized with interest by increased contributions over the ensuing fifteen years. The Internal Revenue Service normally requires that the entire amount waived become due and payable upon plan termination.

Although the Internal Revenue Service is charged with approving or disapproving waiver requests, the Pension Benefit Guaranty Corporation (PBGC) also has an important stake in these decisions. If a plan terminates with insufficient assets, the PBGC is responsible for promised benefits up to the insured limit; the amount the PBGC is called upon to pay out increases if the plan sponsor cannot repay the waived contribution when the plan terminates. To the extent that funding waivers increase PBGC liabilities, they are paid for by the remaining firms in the defined benefit system through higher insurance premiums.

The IRS consults the PBGC on waiver requests involving more than \$50,000 although it is not required statutorily to do so, and it has imposed conditions, such as cessation of benefit accruals and immediate repayment of waived amounts if a plan

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terminates, to protect the PBGC. However, the PBGC believes that this informal role is not sufficient to protect plan participants and the pension insurance system; it is seeking additional protection in the form of new waiver rules as part of the Administration's single employer pension amendments which principally request an increase in single employer pension insurance premiums.

The IRS believes that the current standard for granting funding waivers strikes a proper balance between protecting the interests of plan participants and permitting appropriate funding adjustments for employers faced with financial hardships.

Experience with Waivers

The number of waiver requests increased dramatically from 125 a year in 1978 and 1979 to 1,003 in 1983 and 812 in 1984. Most waiver requests that are not withdrawn are granted, but many firms withdraw formal requests for waivers when it becomes clear the waiver will be denied. Although the debate over funding waivers has focused attention on the percent of waivers that are granted, this statistic may be misleading. It is more an indication of the uncertainty over the outcome of funding waivers than a measure of the stringency of the standards for granting funding waivers.

There are three important issues meriting the Council's attention in considering funding waivers:

1. Effect on the Survival of Firms

Since most waivers have been granted within the last few years, it is too early to conduct an analysis of funding waivers based on outcomes; the fate of most recipients is yet to be determined.

The IRS does not grant funding waivers if there is no prospect that an employer will survive. The Service is under pressure to grant funding waivers where survival probabilities are low because of the possibility that a waiver denial may contribute to an employer's failure and a loss of jobs. The IRS is also sensitive to the possibility that a waiver denial may cause an employer to terminate its pension plan.

There is no disagreement that minimum funding waivers have helped some firms to survive during periods of economic hardship, but the precise relationship between waivers and survival is unclear since minimum funding waivers are typically one of several forms of transition assistance that firms seek during such periods, e.g. private sector borrowing and consolidation of

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assets. The PBGC argues that the trend in waiver requests suggests that firms increasingly are relying on minimum funding waivers to ease their financial difficulties because they are repayable over 15 years at below market interest rates. The IRS notes that the trend in waiver requests reflects changes in economic activity.

2. Incentives for Establishing and Maintaining Defined Benefit Pension Plans.

Minimum funding waivers were included in ERISA by Congress as an alternative to a firm's terminating its pension plan during a period of economic hardship. The IRS argues that making it more difficult for firms to obtain waivers would create a disincentive for the establishment and maintenance of defined benefit pension plans.

The PBGC does not agree that reforms in the procedure for granting waivers will reduce the overall willingness of firms to establish and maintain defined benefit pension plans. It notes that funding waivers are requested by a very small segment of the pension plan "universe" (about 1,000 of the 200,000 defined benefit plans request a funding waiver each year). The effect of reforms of the waiver process on pension insurance premiums must also be considered. The reduced premium that would result from reforms could encourage the growth of defined benefit plans.

3. Impact on the Pension Insurance System

Although it will be many years before the actual losses to the PBGC from outstanding funding waivers are known, the PBGC is concerned with the potential losses that could arise from plans that have received waivers totaling several hundred million dollars. They are also concerned with several large requests that are pending before the Internal Revenue Service.

Minimum funding waivers granted to date have increased the liabilities of the single-employer pension insurance fund by approximately \$67 million. However, approximately one-third of these liabilities are attributable to waivers that the IRS granted in concurrence with the recommendations of the PBGC. This figure does not reflect that some plans may not have terminated because of waivers thereby reducing the PBGC's liability.

An important interest that may not be adequately represented by current procedures is that of plan sponsors who are not in financial distress. These plan sponsors bear the cost of funding waivers that are not repaid because terminations of underfunded plans increase the premiums required to maintain the solvency of the PBGC trust fund. The fund has a current deficit of over \$462

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million.

Options

The Working Group on Pension Policy has discussed the general question of funding waivers and, working with the IRS and the PBGC, is examining a number of alternatives to the current procedure. One issue, however, requires the Council's immediate attention: whether the Administration should include as part of its proposed amendments to the Single-Employer Pension Act a provision providing a statutory lien in favor of the pension plan when the IRS grants a plan sponsor a waiver of its minimum funding obligations.

The PBGC proposal would treat the amount of a waiver as an immediate "debt" of the plan sponsor to the plan. The debt would be secured by a lien (with the priority of a tax lien), which the PBGC could perfect and enforce.

Option 1: Delete from the Administration's draft amendments to the Single Employer Pension Plan Act the provision providing a statutory lien in favor of pension plan participants at the time an employer is granted a minimum funding waiver by the IRS.

Advantages

- o This option retains maximum flexibility for the IRS in facilitating funding adjustments for employers facing financial difficulties.
- o An unencumbered funding waiver provides a viable alternative to some firms terminating their pension plans during periods of economic hardship.

Disadvantages

- o The current system may not provide adequate protection to plan participants or the pension insurance fund since the PBGC which has no formal role in decisions to grant or deny minimum funding waiver requests.
- o The current system of not providing protection to the PBGC through a lien or other measure increases the PBGC's liabilities and necessitates increased premiums for all pension plan sponsors.

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Option 2: Include in the single employer pension legislation statutory authority for the IRS to impose a lien at its discretion as a condition for granting a waiver.

Under this option there would not be a presumption that a lien would be required as a condition for granting a funding waiver, but it would simply be one of several conditions that the IRS might choose to impose. The new provision could provide that, once the IRS decides to impose a lien, the PBGC would have full authority to perfect, administer, and enforce the lien (including negotiations for alternative ways to satisfy the lien through a bond or other security device).

Advantages

- o This would provide some additional protection for the pension insurance system while maintaining a good deal of flexibility for the IRS in granting waivers.
- o This would permit the IRS to use liens only in those instances when they are convinced it would not exacerbate the firm's financial problems or otherwise disrupt normal business practices.

Disadvantage

- o Selective use of liens would provide only partial additional protection for the PBGC from increased liabilities arising from funding waivers.

Option 3: Include in the Administration's single employer pension legislation provision for a statutory lien in favor of pension beneficiaries which would be administered and perfected at the discretion of the PBGC.

The provision would include authority for the PBGC to exempt a firm from the lien provision in exceptional cases where such a provision would greatly disrupt or aggravate a firm's financial difficulties. Such waivers from the lien provision would, however, be the exception rather than the rule.

Advantages

- o This would provide a good deal of additional protection

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for plan participants and the pension insurance system while still permitting flexibility to waive the lien requirement in exceptional cases.

- o This would provide a basic change in the current pension insurance system and may satisfy key interest groups that have made measures to limit PBGC losses a condition of their support for the premium increase.

Disadvantages

- o This provision could reduce some firms' willingness to establish and maintain defined benefit pension plans.
- o Excessively rigid application of a statutory lien requirement could cause adverse credit and financial consequences for firms during periods of economic hardship leading some firms to fail or terminate their pension plans.

Option 4: Introduce legislation to transfer the authority for granting minimum funding waivers from the IRS to the PBGC.

Advantages

- o This would provide the greatest protection for the pension insurance fund and a mechanism for balancing the concerns of parties that are affected by minimum funding waivers.
- o This would take advantage of the incentive for the PBGC to preserve firms so they do not terminate their pension plans and their incentive not to grant waivers to firms who are likely to fail.

Disadvantages

- o It is likely that such a transfer would reduce the number of funding waivers granted and the contribution this form of assistance makes to firms in financial difficulty.
- o At the present time, there is little legislative support for such a change.